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Mitigating the Social Impact of Privatization and Enterprise Restructuring

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Executive Summary and Acknowledgements

This paper focuses on the role the social sectors play in the economic restructuring. Restructuring often results in significant downsizing of labor. When this occurs a negative social reaction can slow and/or stall restructuring. This is increasingly recognized by development agencies, governments, and enterprise managers and as a result social programs are increasingly becoming part of the design of enterprise restructuring programs.

There are economic, social and political objectives for providing social support packages (SSPs) to workers displaced by restructuring and privatization of State Owned Enterprises (SOEs). Social support programs should include elements that combine to “pull” and entice excess labor to leave overstaffed enterprises, while at the same time helping “push” and assist displaced workers to quickly rejoin the labor market. These measures usually include both temporary income support and active labor programs. To be effective the measures must be carefully designed and targeted, and social monitoring of displaced workers should be an integral part of the design to ensure the services are reaching the most needy workers.

Most successful programs include direct dialogue between key stakeholders (e.g., the government, enterprise management, workers, and community leaders) both before and during the restructuring program. The design of SSPs, while based on some generic principles, must be country-specific. The process of divestiture of labor, and related social assets, has three major elements including enterprise analysis, pre-layoff assistance, and post-layoff services.

There are a range of alternative post-layoff services. Income support packages should be examined as to timing, level of support, and how it can be integrated into a package that is affordable, limits abuse, does not have overlapping components that allow double payments, and is targeted in a manner that will protect the most vulnerable and not encourage long-term unemployment. The range of labor redeployment services include those that address frictional unemployment, structural unemployment, and lack of demand for labor. Appropriate design, administration and targeting of these programs are critical if they are to have a significantly positive net impact on employment and wages.

Evaluation and monitoring of activities need to be built in as an integral part of any social mitigation activity related to privatization and restructuring. In undertaking evaluations, the social, political, and economic objectives of the programs need to be taken into account. The key objective of social mitigation is to ameliorate the short-term negative impact of adjustment on individual workers and help them get back into productive employment as quickly as possible. However, it must be stressed that jobs are created by investment and a growing economy, not by labor services. Labor services can help mobilize appropriate human capital, but not create jobs in and of themselves.

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Mitigating the Social Impact of Privatization and Enterprise Restructuring

David H. Fretwell*

I. BACKGROUND

This paper focuses on the central role the social sectors play in the restructuring process. During restructuring there is often significant downsizing of labor and when this occurs the social impact and reaction can be such that restructuring is slowed and in some cases stalled. This fact is increasingly recognized by development agencies, governments, and enterprise management and as a result social programs are becoming an integral part of the design of enterprise restructuring programs. To quote the former Minister of Finance from Macedonia *'we cannot and will not proceed with privatization of large state owned enterprises unless we have a program of targeted social support in- place for the affected workers'*.

There are generally three phases in the process of divestiture of labor and social assets: the *decision phase*, which culminates in the governing board or government ordering the enterprise to start labor negotiations based on agreed reduction/divestiture of the business plan of the enterprise; the *urgent divestiture phase*, which starts when the decision has been taken to initiate labor negotiations, and is completed when the revised business plan is updated with related divestiture of labor, equipment and land; and the *development and renewal phase*, which overlaps with the urgent divestiture phase and will extend over several years.

The *decision* and *urgent divestiture* phases create within the affected communities feelings of threat, anxiety and uncertainty about the future. As a result, labor representatives often ask for a reconsideration of divestiture, which leads to a prolongation of unprofitable activities at the enterprise in question. Therefore, it is desirable that social support programs

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be defined at the outset and as part of the overall divestiture process, and that the *development phase* starts as soon as possible to create confidence in the future.

Divestiture of labor and social assets during enterprise restructuring and privatization is an ongoing activity in both developed and developing countries. Support for divestiture, through social mitigation programs, has and continues to be supported by the World Bank as well as other development agencies. This paper attempts to briefly summarize some of the experiences in the World Bank, particularly those since 1990 when extensive enterprise restructuring began in Europe and Central Asia. The paper is intended to serve as a “checklist” by Bank staff and borrowers during the design of social mitigation programs during enterprise privatization and restructuring. It is not designed as a detailed technical research paper, but does refer to a number of related technical papers and countries where the Bank has and continues to be involved in supporting divestiture (e.g., Turkey, Russia, Poland, Macedonia, Romania, etc.). The reader is encouraged to follow-up and review these technical references, as needed, to gain more insight into particular issues, and the pros and cons of different approaches.

Objectives of Social Support Programs

There are economic, social and political objectives for providing social support packages (SSPs) to workers displaced by restructuring and privatization of State-Owned Enterprises (SOEs). From an economic standpoint the objectives are to reduce excess labor costs so enterprises can be competitive, and to facilitate the rapid return of workers to productive employment and thus reduce the duration of state-supported income support payments. From a social standpoint, the objectives are to provide transitional income support while displaced workers are finding alternate employment and, for those who have difficulty finding employment, provide extended income support to prevent these workers and their families from slipping into poverty. From a political standpoint social support programs are intended to build public support for restructuring by signaling to citizens, communities and labor representatives that those responsible for restructuring are attuned to the needs of affected workers and that they are ready and willing to assist those that need and want help.

Social support programs should include elements that combine to “pull” and entice excess labor to leave overstaffed enterprises, while at the same time helping “push” and

assist displaced workers to quickly rejoin the labor market. These measures usually include both temporary income support and active labor programs. To be effective, the measures must be carefully designed and targeted. Furthermore, there should be continuing social monitoring of displaced workers to ensure the services are reaching the most needy workers and the most vulnerable are identified early and provided with special assistance as needed.

International Experience

Many countries around the World have and are implementing economic restructuring and recovery programs (Fretwell, 1995; Hoeven, 1997; Kikeri, 1998). Some are directly linked with privatization of SOEs (e.g., in transition economies in Eastern Europe and Central Asia), while others (e.g., North America and Western Europe) are part of an ongoing process of economic change and renewal. However, the design and use of social support programs varies considerably between countries and is greatly influenced by the economic environment, including the level of unemployment, and type of general social support programs already in place in the country where economic restructuring is occurring. A review of 12 case studies of enterprise divestiture in Europe, Latin America and Asia indicated that workers as a class did not lose by divestiture, but that individual workers could be worse off especially where layoffs or reduced hiring were involved (World Bank, 1992). Unfortunately, this is the environment in which divestiture often occurs, and why temporary social support programs are instituted to mitigate the social impact. A brief survey of a sampling of such programs follows:

- *Latin America: In Brazil*, a varied set of income support and other support packages were used to retrench workers between 1995 and 1997 in six SOEs, including three banks and three utilities. A parallel program was carried out by several states. Severance payments were a core element of the program, plus extended medical benefits, retraining, help for business startups, and job search assistance to affected workers. Economic restructuring in Latin America was sometimes carried out in a manner and in an environment that increased employment, thus making divestiture more palatable to labor. For example, *in Chile*, employment in 10 state owned companies privatized between 1985 and 1990 increased 10% because of overall headway achieved in economic growth and investment by the firms involved

(Larroulet, 1992). *In Argentina*, starting from a base of 222,000 employees in 13 major public enterprises in 1990, employment was reduced to about 42,000 by 1993 via transferring 66,000 workers to private firms, retiring 19,000, and providing 95,000 with severance payments. The advanced age of many workers, generous severance, multi-job holding phenomena, reactivation of the economy and expanding labor market are credited for producing a lack of opposition from labor (World Bank, 1993; Guasch, 1996).

- *Western Europe: In Germany* a new institution, the Ttruhandanstalt was established to deal with rapid privatization of some 8,000 state companies, with a workforce of 4.1 million. The privatization program had an immediate and severe impact on employment. Labor reductions were achieved by early retirement, job placement in new private firms, employment creation schemes including wage subsidies, public works, and retraining; plus unemployment benefits. Special employment companies and counseling services were also established to employ and retrain workers. *In the UK*, British Coal divested a total of 204,000 workers, mostly over the age of 50, who accepted lump sum redundancy payments. In addition, British Coal Enterprise Ltd. was established to assist employees in the sector, and their families, in developing skills and securing new employment with a special emphasis on helping displaced workers start small businesses. *In Sweden*, the Uddevalla shipyard was downsized via normal turnover, early retirement, a freeze on recruitment, and assistance with job search and retraining. The KLAB mine was downsized by normal and early retirement, severance, and retraining.
- *In Eastern Europe*: Privatization in transition economies often took place in a difficult environment where the economy in contracting, and unemployment rising. In Poland, restructuring in the Coal Sector was supported by a Miners' Social Package which included lump sum payments, early retirement assistance, combined with active labor programs (e.g., small business assistance, counseling, retraining) and local economic development assistance to affected communities. *In Macedonia*, severance payments were combined with active labor programs to assist workers affected by restructuring of 25 large loss-makers. Approximately, one-third of

affected workers participated in the latter services. An added complication in the transition economies is the fact that often a large number of community services (e.g., schools, hospitals, heating, housing) are connected with state enterprises; and when these enterprises are liquidated or downsized these social assets must be disbursed in a manner that would ensure that essential community social services are maintained. *In Turkey*, a generic job loss compensation package is defined in the Privatization Law, and this is supported by a broad array of active labor redeployment programs and related social monitoring activities.

In summary, even the brief review presented in the preceding paragraphs demonstrates a broad range of social support programs. However, most successful programs include direct dialogue between key stakeholders (e.g., the government, enterprise management, workers, and community leaders) both before and during the restructuring program. The stress and emphasis on income support (e.g., severance) vs. other forms of support (e.g., labor services) vary depending on economic and employment conditions, but most programs include both elements to varying degrees. Any new SSP should draw on this and on worldwide experience, and must be designed in a manner responsive to current conditions in a specific country. Finally, enterprise restructuring is not a “one-off” process. Enterprises in the most developed economies must continue to reinvent and restructure themselves in response to changing economic and market conditions worldwide. As such, developing countries need to develop SSPs that have both short and long-run applications

Country Setting

The design of SSPs, while based on some generic principles, must be country-specific. There are a number of factors which must be taken into account in the design, including:

- *Political Commitment*: Is there sufficient political commitment to move forward with the privatization and restructuring program? If there is no political commitment, resources allocated to SSPs may never be utilized because privatization and divestiture of excess labor may never occur; or if it does, workers may be rehired and the funds expended on SSP may be wasted. Furthermore, without political

commitment the SSPs may be too generous as to mute any opposition that it is not affordable.

- *Status of the Economy:* It is easier to undertake privatization and restructuring when the economy is improving, investment is increasing, and unemployment is declining. The worse the economic situation the more political commitment is needed and the more carefully the social package, including temporary income support, must be. The selection of the sectors or enterprise to initiate privatization may also be affected by the state of the overall economy, or the state of a particular sector. For example, if there is a glut of energy (i.e., coal) in the international market, it may be a difficult time to privatize mining, but this may not affect the transport sector (i.e., railways).
- *Multi vs. Individual Sector SSPs:* The preferred approach is to create a generic multi-sector multi-region approach to the design of SSPs (ie.g., Turkey and Macedonia). This helps ensure equity between sectors and regions, and helps prevent high cost SSPs being negotiated with a very strong sector (e.g., coal), which may set unaffordable precedents that cannot be financed in sectors as has been encountered in Serbia and Romania. However, the multi-sector approach may not always be possible. If a multi sector generic SSP cannot be negotiated, it may be necessary to design the SSP sector by sector (at least for the income support/severance components). Fragmented sectoral SSPs can also cause other problems with labor redeployment components (e.g., duplicatory administrations, overlapping programs, lack of critical masses of clients for selected services).
- *Mono-Enterprise Communities:* Enterprises restructuring mono-enterprise communities require special attention, particularly when they are isolated geographically. In these situations, consideration must be given to the provision of SSP relocation assistance, and local economic development planning and implementation grants.
- *Availability of Temporary Income Support:* SSP design must take into account the existence, or lack of, a range of income support programs. Absence of regular social assistance or unemployment benefit systems will directly affect the type of severance packages, as well as active labor programs offered. Wage arrears provide a special

problem, as they normally have first priority for funding. If arrears are large, there may be insufficient resources to finance other forms of income support and labor redeployment programs.

- *Availability of Labor Redeployment Programs:* As with income support programs (if they do not already exist or the ones that do exist are weak), there will be problems with rapid implementation of SSPs. SSPs are normally rapid moving programs, and there is little time for months and years of “institutional development”.
- *Labor Code Issues:* Existing regulations for layoffs and severance may not allow excess labor to be divested in a rapid manner, or if layoffs are allowed the cost of the layoffs may be unaffordable (e.g., in one country displaced workers were entitled to two years severance pay if they were technological surplus, plus two years of unemployment benefits, plus severance). This is not affordable, and in such cases it may be necessary to change related laws prior to privatization.
- *Level of Unionization:* Strong trade unions can be an ally or adversary, depending on their view of the legitimacy of the process and the design of the SSP. They may also be linked with the political opposition and therefore affect the political commitment of the Government. The best approach is regular and upfront communication and involvement of labor representatives in SSP design. In addition, it is critical that an objective public information campaign is launched by the entities designing and implementing the SSPs to ensure that everyone (including displaced workers) gets correct information, and it is not filtered through third parties who may not fully understand the SSP or have specific reasons for providing disinformation

Stakeholders

SSP design requires the involvement of a number of stakeholders. While this would appear logical, it is not always done. In many cases, the entities dealing with privatization and enterprise restructuring (i.e., privatization agencies, enterprises) simply think their job is to create a business plan and/or sell the enterprise and divest excess workers who are expected to fend for themselves and/or access existing Ministry of Labor social support programs. This approach can create immense political and social problems that can slow and stall privatization. In addition, the types and resources for SSPs for workers displaced from

SOEs may differ from those provided to the general population of unemployed (e.g., the workers are older and more experienced, and may not be as mobile as first time workforce entrants). Large scale displacement workers during privatization can overwhelm the administrative and fiscal resources of Ministries of Labor and may have a devastating impact of local communities.

As such, for political, social and economic reasons, it is critical to involve enterprise management, labor representatives, community leaders, and all levels of government, non-government organizations, and the private sector in the design and implementation of SSPs. Some stakeholders may take a leadership role in design (e.g., National Government, Union and Employer Representatives); others may play a role in both design and implementation (e.g., unions), and still others may play a primary role in delivery of services (e.g., local government, community, labor agencies, the private sector, and non-government organizations). The key issue is that major displacement of labor affects an entire community, and everyone has a stake in addressing the problem.

Summary

In summary, workers generally as a group may not lose by privatization and restructuring; however, individual workers may temporarily be worse off where layoffs or reduced hiring is part of the restructuring process. The key question is how to ameliorate the short term negative impact of adjustment on individual workers and help them get back into productive employment, while at the same time recognizing that jobs are created by investment and a growing economy, not by labor services. Labor services can help mobilize appropriate human capital, but not create jobs in and of themselves. Moreover, not all workers can be placed back into the labor force - particularly older, lower-skilled workers - and the best that may be expected may be providing a bridge to retirement with income support or temporary employment programs.

II. PROCESS OF DIVESTITURE OF LABOR AND SOCIAL ASSETS

General Approach to Divestiture

There are several approaches to dealing with divestiture: (a) let the new investor deal with them; (b) have the government assist prior to sale; or (c) combine both approaches.

Investor Driven Layoffs: This approach is one in which the new investor will restructure the enterprise and address related labor requirements. This assumes that the will sell the enterprises at a discounted price, if necessary, and let the new owners deal with the restructuring and related layoffs. This is the preferred option as the new investor is in the best position to know and plan the labor requirements of the enterprise he is buying. Under this option, there is no government participation in the administration and financing of temporary income support and related labor redeployment programs.

Government Assisted Layoffs: The abovementioned approach may make some SOEs very unattractive to buyers, because of large excess numbers of workers. Therefore, the government may become involved in designing, financing, and administering the divestiture process prior to and during privatization and restructuring. The buyer may have other investment alternatives, in other parts of the world, and may not want to get involved laying off large numbers of workers in a heavily unionized environment immediately after purchasing an SOE. In addition, unions may not view the basic severance option under the Labor Law as sufficient reimbursement for layoffs when alternate employment is not easily available. The Privatization Law may address this issue by providing a framework for additional support and labor redeployment services to SOE employees displaced by restructuring. If these programs are made available before sale and with government support, some labor may leave voluntarily, the SOEs may become more salable, social issues will be addressed, and the reaction of labor may be less negative and strident. The government may, in fact, be able to rapidly recapture the cost of any social support programs provided prior to sale by gaining a higher cost from the sale.

Notwithstanding the approach taken, the process of divestiture of labor, and related social assets, has three major elements¹, as follows:

- *Enterprise Analysis.* To identify existing enterprise personnel to be affected by privatization and restructuring decisions and social infrastructure to be divested;
- *Pre-Layoff Assistance.* To develop labor adjustment plans for workers prior to dismissal; and
- *Post-Layoff Assistance.* To provide temporary income support and labor redeployment services to individual displaced workers and support regional development efforts.

Enterprise Analysis

Three broad issues, vital for the process of divestiture and restructuring, are addressed from the standpoint of the key stakeholders concerned (i.e., enterprises, trade unions/labor, and the government). The key issues are (see Table 1 for summary): (a) divestiture of labor, how to define the level of labor divestiture to meet productivity goals in enterprises to be privatized and/or restructured; (b) labor regulation, how to identify external and internal labor/union regulations that affect labor divestiture; and (c) divestiture of social infrastructure, how to identify social infrastructures that can be divested and the alternatives for doing so (Fretwell, 1995).

¹ The elements should be addressed in a sequential fashion; however, in reality they are overlapping and in some cases the first two elements may not be addressed in-depth if layoffs begin quickly with very little forward planning

Table 1: Role of Stakeholders in Divestiture of Labor and Social Assets

| CONCEPT | STAKEHOLDER | ISSUE |
|-----------------------|-------------|---|
| LABOR DIVESTITURE | Enterprise | Business/labor plan, skill analysis |
| | Government | Regulations, information, Temporary income support programs, Labor redeployment services |
| | Unions | Negotiations, agreements, qualifications, education, training |
| LABOR REGULATIONS | Enterprise | Regulations, negotiations, agreements |
| | Government | Regulations, negotiations, monitoring industrial relations activities, support for new employment projects, small business development |
| | Unions | Acting on behalf of employees regarding application of regulations, negotiations |
| SOCIAL INFRASTRUCTURE | Enterprise | Divesting assets and activities. Selling or giving away to private persons or government. |
| | Government | Encouraging employees and communities to take-over |
| | Unions | Taking responsibility for selected social services such as schools, housing, health care. Support employees willing to take over social assets. Assist employees in purchasing social assets (e.g., housing, assets with commercial potential) |

Defining the Level of Labor Divestiture: The role of the enterprise or new investor is to select the correct mix of labor to keep and to divest. There are several approaches to determine the level of labor divestiture. Very often the decision on divestiture has been taken by the government and comprises a total closure of a plant, but there are also partial closures and partial divestitures. In such cases labor divestiture could begin before privatization, particularly if the government "commercializes" the SOE and weans it from State Budget Support. If this is done the SOE often experiences its first round of labor divestiture, and

implements the easier or "soft" reductions in order to improve cash flow. By the time full divestiture and privatization occurs (i.e., the transfer of 100 percent of ownership and control to the private buyer), the SOE is often left with staff who for various reasons (e.g., age, skills, dependent responsibilities) are more difficult to layoff. In any case, labor divestiture generally involves the following elements:

- *Business plan.* After having defined the new business plans of the enterprise regarding market, products and volumes, the organization and utilization of labor must be defined to reach desired efficiency.
- *Efficiency.* The new enterprise must become as good as or better than the competitors. Organization and employment levels should be compared with the situation in competitor enterprises to provide an indication of needs.
- *Skill and competence analysis.* After the reorganization plan is presented, the qualification requirement is then identified. An analysis of the skill and competence of the existing personnel must be performed. People meeting the new requirements will be selected from the existing staff. Remaining personnel has to be divested and/or retrained. For divestiture in Formerly Centrally Planned Economy (FCPE) countries it will be necessary to educate managers to undertake new management responsibilities, or recruit new managers with experience from private enterprises. It is important that the new management has both the right qualifications and the understanding of private business.
- *Temporary income support and measures to facilitate labor redeployment.* It is likely that restructuring and privatization will be followed by divestiture of labor. Action must be taken to provide support service to all redundant personnel who may request assistance. Local and national governments and enterprise management have to cooperate in order to use every opportunity to redeploy redundant personnel (these topics are covered in detail in Section III of this paper).

Identifying Labor Regulations Affecting Labor Divestiture: Freedom of action for divestiture of labor is often limited by legal and financial restrictions. What the enterprise management can do, however, is to try to get laws and regulations changed and/or to reach an agreement with the unions on the implementation of the regulations. There may be two types

of regulations affecting labor divestiture: (a) external and national legislation; and (b) industry and/or sector specific internal tripartite collective agreements. Both may need to be addressed.

- *Examine existing regulations:* Regulations regarding external agreements normally are negotiated between employer organizations and labor unions; are known to the enterprise management; and may be embodied in national legislation. Internal regulations are agreed within the enterprise and known to management and unions. These provide a formal framework for the divestiture. Enterprise management has to identify regulations that serve as obstacles to the divestiture process. The implementation of the regulatory framework could also be an obstacle to divestiture. However, implementation of internal rules and internal regulations may be re-negotiated with labor unions at the enterprise level.
- *Labor Negotiations:* The rules can be very different, even between sectors within countries. It is, of course, an advantage for the employees to remain employed as long as possible, even if divestiture must follow. If the projected results of divestiture are positive, but the rules prevent it, new labor negotiations must take place. Open information and a presentation of the consequences of the non-event of the divestiture should be used to help persuade the unions. If the blockages are with external national regulations the government may need to review them and take appropriate action. If the impediments are internal to the sector or enterprise, then the collective bargaining agreement may need to be renegotiated. One problem that may arise in this situation is a lack enterprise management expertise in renegotiating such agreements, particularly in FCPE countries.
- *Setting Legislature in Place:* There are examples of regulations which can be obstacles for divestiture, that in some cases have stopped the procedure. For example, the Moroccan regulation that no state employee can be fired has been hindering a rapid divestiture of the Jerada mine. Another example was the complicated priority order for dismissals in the Former Yugoslav Republic of Macedonia that became an obstacle for labor terminations. If there is no ground for negotiations, the decisions have to be made by the enterprise without a consensus procedure. If existing laws

and regulations are hindering the divestiture, they either need to be changed or additional regulations need to be put in place. If that is not possible, one approach is to declare the enterprise bankrupt, and then restart without any obligations.

Identifying Social Infrastructure to be Divested. In middle-income countries and in FCPE countries, assets such as schools, houses, health services, water and energy supply systems are often run by SOEs. In the restructuring and privatization process those assets have to be sold off to private companies or individuals, or responsibility shifted to local or other government authorities before the privatization can take place. It is unlikely that private owners would take over assets that could not provide a sufficient return on their investment. New investment capital needs to be concentrated on competitiveness and the turning of losses into profit. The following issues need to be addressed:

- *What assets?* The management of the enterprise has to investigate how they can divest social assets. Schools, health care, housing, transport, water and energy supply systems are social activities which may not be handled by private enterprise.
- *Different methods of divestiture.* When enterprises are responsible for schools, housing, health care, etc., it is often in small communities where they have been the dominant employer. In an effective new enterprise, management must leave all unusual responsibilities and concentrate on the core business. There is no special method for divesting this type of assets but the key constraint is the ability of local and national governments to take over these responsibilities in a line of shrinking budgets.
- *Negotiations.* Negotiations with the local government must be positive, and financial support can be offered for the change-over period. In a small community where the enterprise is dominant, it is not necessary that all social assets be divested. They can be operated in the most economic way. If it is very costly for the community, the enterprise may have to share the expense in a diminishing way over time.
- *Valuation.* The value of the social property and activities must be determined, and the property should be sold to the private sector and/or individuals (e.g., hotels, housing) or given (e.g., schools, clinics) to the local government. However, this may have significant ramifications for the tax base of local and national governments and for

the enterprises. The impact needs to be calculated in a total perspective. The enterprises, as well as the inhabitants, have to pay taxes for the public service.

- *New Owners.* The rules have to be established by the original owner, normally the government. In the divestiture process it is of common interest to both the old and the new owner to get optimal use of the social assets. Among interested new owners or "customers" there will also be employees and former employees. If the customer is a private person or business, normal business negotiations have to take place. In this case, it is the responsibility of the unions to try to safeguard the interests of the workers.

Each proposal for privatization should contain certain basic information on social assets including: (a). information about the way the State acquired the property; (b) assessed value of the property; (c) if a commercial company is to be founded, its legal form; (d) if a joint-stock company is to be founded, description of the method for dividing the shares, the types of shares or investment vouchers and their percentages; (e) in the case of sale, its form and method for determining the price and conditions of payment; (f) operating costs, if the municipality is going to take over, for example, a health clinic; and (g) a schedule for the realization of each sale.

Pre-Layoff Assistance

Background: The basis for pre-layoff notice - specifically for large-scale layoffs and services - needs to be established as it is a first step in promoting smooth adjustment (OECD, 1998), and is particularly important in mono-enterprise communities. The period between the decision to restructure and the time workers are actually to be displaced is one of the most difficult for those affected. In order to reduce social tensions it is critical that workers are clearly informed of the options and services they may be provided with if they are laid-off (e.g., temporary income support, active labor programs). This process, sometimes referred to as Industrial Adjustment Services (IAS), should involve collaboration between labor, enterprise and government with the objective of starting services for workers before they leave the plant. Such investments have proven quite cost-effective and help prevent displaced workers from falling into long-term unemployment. When it is a question of total divestiture and closure of a plant - and all the employees will be affected in a similar way -

the situation, in a way, becomes easier to handle for the unions. On the other hand, in a situation when some activities are going to survive and others not, the situation is more complicated.

Legal Basis: The length of notice, and financing of services, need legal definition and supporting regulations. Longer periods of notice are preferable to shorter periods; as evidence suggests, notice of only two or three weeks has negligible effect on shortening periods of unemployment of displaced workers because this does not allow stakeholders to mobilize support. Furthermore, contrary to a common misconception, there is no evidence that productivity of the workforce is adversely affected during a notification period (U.S. Department of Labor, 1986); in fact, there is some evidence to that workers become more productive, as they want to demonstrate that they do not need to be displaced. Different periods of advance notification for large-scale layoffs are found, usually varying from 30-90 days, and the notifications include definitions of large scale layoffs. The definition of “large-scale” needs to be done carefully, and regulations usually combine a proportion of the labor force of a particular enterprise (e.g., 10%) with a minimum number of workers (i.e., 100 workers in a particular location). The size of the qualifying layoff may vary by the size of the community where the enterprise is located. It is not useful or administratively workable to initiate specialized services for very small numbers of displaced workers who can probably be handled by normal services for the unemployed.

Services: Typical services include: (a) establishing eligibility and assessing the interest of workers in temporary income support and labor redeployment programs; (b) worker skill audits; (c) provision of initial in-plant job counseling and placement services; and (d) provision of public information on restructuring. The evaluation material shows that the delivery of services works best onsite where the displacement will, or has occurred (OECD, 1988). Rapid response is critical, and the most successful services involve the transfer of authority onsite to the local level to bring the employer and local community into the structure. The Canadian IAS is one example of these services. Similar services have been developed in other countries (e.g., Poland and Hungary). IAS services are small units, sometimes located in National Employment Services, that are composed of specially trained staff as advisors who, on request, provide assistance to firms and communities that are facing

large-scale layoffs. Experience in the OECD and developing countries indicates that the returns to small amounts of resources for IAS are cost-effective in terms of shortened periods of unemployment among displaced workers. The IAS need to focus on the most vulnerable labor markets and ensure that public funds are used in the most efficient way, that all local stakeholders are involved and work together to solve practical labor problems, and demonstrate to the worst-affected that both the community and government care about the problems of adjustment.

III. POST-LAYOFF SERVICES

Objective

The overall objective of these services is to provide temporary assistance to displaced workers while they are unemployed and to assist the unemployed in re-entering the labor market as quickly as possible. As mentioned previously, there are basically two types of services: (a) temporary income support; and (b) labor redeployment services. The assessment for the demand of these services should be accomplished during the pre-layoff steps described in Section II of this paper. It is critical that leadership for organizing the services, developing necessary administrative framework for implementation, and obtaining necessary financing is completed during the pre-layoff stage. Public information about the nature of the services, for displaced workers as well as service providers, is also important. Above all, care should be taken during the pre-layoff stage not to advertise services that cannot be delivered, as this will add to, and not reduce, social tensions. In defining and advertising the services several key questions must be addressed, including:

- What services are currently available;
- Which of these services can be rapidly expanded;
- What services can be added;
- Who will deliver the services;
- What will be the cost of these services;
- How these services can be targeted in a manner that will make the most cost-effective use of public funds; and

- What type of evaluations should be done to improve the impact and cost effectiveness of the services.

In making decisions on the above issues, it should be noted that there is no one program or service that is the most effective for all clients, or in all settings. The lowest unit cost service may not be the most cost effective, nor may the highest cost intervention for specific group of clients. In short, different clients will benefit from and want different services. The key is to target the services. Finally, if there is no need to assist displaced workers, then do not assist them, as doing so will simply reduce resources available for other more vulnerable clients.

Income Support Programs

Income support programs that support economic restructuring normally combine the type of programs that are available to the general unemployed, along with special programs that are designed to “entice” or “pull” labor out of enterprises undergoing restructuring. While each situation is unique, there are a range of programs that are being used. The final design depends on such factors as: general economic conditions; general level of unemployment; demographics of the workforce; conditions of remuneration of the affected workers; relationship between representatives of labor, state, and enterprise management; and the role of the enterprise in the country and community. Isolated communities, where one employer dominates, are a particular problem. Income support programs can be quite costly in the short-run (e.g., in excess of an average of US\$10,000 per worker in middle income countries); however, costs can be reduced significantly if displaced workers are able to find alternative employment rapidly. On the other hand, sometimes paying workers “not to work” is less costly than continuing to employ them in loss making enterprises. There are a range of alternatives for income support, each of which should be examined as to timing, level of support, and how it can be integrated into a package that is affordable, limits abuse, does not have overlapping components that allow double payments, and is targeted in a manner that will protect the most vulnerable and not encourage long-term unemployment. The general alternatives are summarized in Table 2, and described in more detail in the succeeding paragraphs.

Table 2: General Types of Income Support and Application

| TYPES OF INCOME | EMPLOYMENT STATUS | | |
|---|-------------------|------------|---------|
| | Employed | Unemployed | Retired |
| Support Programs | | | |
| Wages Arrears | ----- | | |
| Severance | | --- | |
| Unemployment Benefits | | ----- | |
| Social Assistance | | ----- | |
| Early Retirement Social Assistance | | ----- | |
| Early Retirement | | --- | ----- |

- *Wage Arrears:* Wage arrears usually need to be cleared before other types of income support are provided, particularly if some workers are to remain and others are displaced and may be eligible for special severance payments. If wage arrears are large, it can cause major problems and stall the divestiture process if sufficient financing is not available to cover the arrears.
- *Regular Severance:* Many countries have severance programs, and amounts vary depending on length of employment (e.g., 30 days for up to five years service, 90 days over 10 years, etc). Other countries may have a more extensive system that substitutes for unemployment benefits. Turkey had such a system where workers received one month of severance for each year worked up to a maximum of 12 years. These latter systems are theoretically financed by enterprises, but if SOEs enter bankruptcy the government usually becomes liable. Such systems do not promote labor mobility, but do provide some worker protection in the absence of a formal unemployment benefit system.

- *Special Job Loss Compensation/Severance:* These payments are in addition to regular severance, and are designed to “pull” or “entice” more workers to leave - payments range from 1-2 years of salary (depending on conditions and length of service), payments should be made on a lump sum severance basis to encourage investment and not consumption. They normally decline in size over time to increase initial impact. If payments are not made on a lump sum basis it may discourage investment and delay worker re-entry to the workforce, since payments are sometimes stopped if workers take up employment (as in Turkey). An issue that needs to be addressed here is the length of notification of dismissal prior to provision of special severance/job loss compensation payments. A lengthy notification period has the effect of postponing labor divestiture, and the costs need to be calculated because long notification periods may mean that wage and benefit costs will continue to accrue.
- *Unemployment Benefits:* In many countries these are available, but in some they are not. Starting an unemployment benefit in the context of rapid privatization and enterprise restructuring is not usually a viable option, but rather a long-term institutional development program.
- *Social Assistance:* These payments normally act as a social safety net for those who do not qualify for, or have exhausted, regular unemployment benefits. Payments are usually means-tested, family-based, normally at lower level than unemployment benefits, and linked to poverty lines.
- *Early Retirement:* This instrument can have a negative effect on already indebted social security systems. It should be noted that this option may become more expensive than lump sum severance payments if it is extended to many people, and as such should only be applied to workers very near retirement. An alternative is to provide “*social assistance payments*” to workers who are near voluntary retirement age, and/or involve these individuals in “*temporary community employment programs*” until they reach retirement age. This can be done in two ways: (i) as bonuses to workers who reach retirement, providing they retire when they are eligible; or (ii) as payments to workers who are near retirement by providing them some percentage of their existing gross salary (e.g., 75-80%) while at the same time

placing these workers on administrative leave with the understanding that they will formally retire when they are eligible.

- *Individual Pension Accounts:* These payments amount to a contribution-defined pension or unemployment benefit system where each worker deposits a portion of his/her salary in an interest bearing account, and in the case of job loss or voluntary separation he/she can withdraw from the account. Such systems, which are sometimes found in Latin America, support labor mobility, make workers directly aware of the consequences of poor job performance, but may not compensate workers adequately when job loss is beyond their control.
- *Share Distribution:* Another indirect method of providing income support is to provide workers, including those affected by downsizing, with shares of the company. This may also stimulate productivity, but as an income support measure is not viable if the company is liquidated.

Labor Redeployment Services

These programs are designed to help “assist and push” displaced workers back into the labor force to increase overall productivity and decrease use of income support payments. These services support, and need to be coordinated with, income support payments. There is evidence that labor redeployment programs can have a significant positive impact (Fretwell, 1999; Betcherman, Olivas and Dar, 2004) if carefully targeted and well-run (i.e., services are demand driven and delivered by service providers which have performance based contracts). Services are normally used by about one-third of workers and are relatively low cost (e.g., averaging US\$50-1,000 per worker in middle income countries depending on the nature of the service provided) as compared with income support payments (see Table 3 for typical unit costs). It should also be noted that while income support payments are usually directed only to displaced workers, that other affected workers (e.g. family members, secondary layoffs) are often allowed access to redeployment services. This can help produce positive social and political reactions to economic reform programs, at a reasonably low cost. A variety of services is needed to address three conditions commonly experienced by displaced workers who are trying to re-enter the labor market:

- *Frictional Unemployment:* Displaced workers have marketable skills for which there is demand, but they need intensive job placement assistance. These services can have a substantial positive impact on re-employment and have a low unit cost. These services can include assistance for remote job search and relocation at a low unit cost.
- *Structural Unemployment:* Displaced workers lack skills, or their skills are not in demand, and need some re-skilling to compete and re-enter the labor market. Different types of retraining, including on-the-job-training and/or institutional training is needed in these circumstances and can help redeployment at a moderate unit cost per worker.
- *Lack of Demand for Labor:* This is a particular problem in areas of high unemployment and in mono-enterprise communities, that shed large amounts of labor. Programs include small business consulting assistance, incubators, and micro-loans (although the latter may not be critical if substantial severance payments are provided). These programs tend to be *more* expensive than other services, attract a limited number of participants from state enterprises (e.g., 5-6%), but can be quite effective. Temporary Community Employment Programs are also sometimes used and, although the social and infrastructure benefits are recognized, these programs must be limited and carefully targeted to the vulnerable because of the high unit costs and considerable evidence that they have no impact, and often negative impact, on post program employment and wages (Fretwell, 1999). Finally, local economic development planning grants, particularly in mono-enterprise communities, can have a long term impact on job creation and have already been implemented successfully in OECD and Middle Income Countries (i.e., Poland, Romania, Turkey, Macedonia).

**Table 3: Typical Unit Costs Per Client for Labor Programs
(USD - 1998)**

| Type of Program | Czech Republic | Hungary | Poland | Turkey |
|----------------------------------|----------------|---------|--------|--------|
| Employment Services | 12 | 25 | 30 | 17 |
| Training | 265 | 500 | 300 | 200 |
| Public Service Employment | 625 | 1,200 | 800 | N/A |
| Wage Subsidy | 885 | 950 | 560 | N/A |
| Self Employment | 885 | 1,000 | 2,830 | N/A |

Efficient administration these programs, in response to worker demand, are critical to their success. The programs may run in parallel with normal programs for the unemployed, but may have different criteria due to the clientele (i.e. training programs may be longer given the fact that some displaced workers may be high level and need major re-skilling). Complications may arise if labor redeployment programs for displaced workers are administered in parallel by existing labor offices with ongoing programs for the unemployed. First, as noted, criteria may be different. Second, regular programs may not be as responsive as needed. Quick and targeted start-up is critical to serve the needs of displaced workers. Third, the government may want to differentiate these programs from regular programs for political, social, and financial reasons. Fourth, labor office personnel may misinterpret criteria for the new program and force it into an inappropriate mold based on criteria in existing programs. For these reasons it is not uncommon to see a Privatization Agency administering these programs, including contracting with service providers directly without working with or through regular Employment Service offices. Financing options also need to be explored, and one option is to set aside a portion of the proceeds from privatization for labor redeployment programs. Finally, whichever agency administers the programs will be critical to ensure the programs are well publicized and designed to both displaced workers and potential service providers. As such, a tripartite advisory board is normally established to provide policy guidance and promote the programs.

In summary, some key lessons learned from operation of labor redeployment programs include a need to:

- Ensure sufficient financing at the outset so programs do not have to be terminated early with subsequent social and political problems;
- Use performance-based contracting (i.e., negotiate job placement or business start-up rates) with service providers to maximize impact and quality;
- Implement ongoing gross impact evaluations, and infrequent net impact evaluations (see Section IV of this paper);
- Assess and screen applicants before entry to programs to increase impact and cost effectiveness;
- Limit the use temporary community employment programs as their impact on downstream employment may be negligible or negative, and the programs are very expensive. Use other types of income support;
- Be careful in generalizing from research on impact of programs from other countries; instead evaluate ongoing programs and adjust criteria as necessary;
- Realize that well-designed and targeted programs may have a positive net impact, but poorly designed and targeted programs probably will not have any economic impact.

Finally, it needs to be emphasized that labor redeployment programs, in and of themselves, do not create jobs. They help create needed human capital and improve the mobility of labor. But, in the end, it is investment and economic development that creates employment.

IV. EVALUATION AND MONITORING

Evaluation and monitoring of activities need to be built in as an integral part of any social mitigation activity related to privatization and restructuring. In undertaking evaluations, the social, political and economic objectives of the programs need to be taken into account. Consideration should be given to incorporating several types of evaluation into the social mitigation programs:

- *Income support programs:* Normal fiscal and administrative audits need to be completed for all programs to ensure payments are going to eligible persons. Audits

should include matching of individual worker records between programs, and if possible, to identify individuals who may be getting illegal duplicate payments (e.g., they are on unemployment benefits and getting a salary as a participant in a temporary community employment program). A decision also needs to be made if workers who get special lump sum severance payments automatically become immediately eligible for additional unemployment benefits. Normal practice is to delay eligibility (e.g., if a person gets two years of special severance, eligibility of normal unemployment benefits may be delayed for 6-12 months). Special attention also needs to be paid to the disbursement of severance payments to workers, particularly if the funds are provided to the enterprise, which then makes payments to individual workers. Finally, there needs to be an audit of any “rehiring” of workers at the enterprise from which the worker was displaced. This can often be done by matching worker identification numbers with pension or employment registration data.

- *Follow-up on Displaced workers:* Regular (e.g., every six months) sample follow-up on displaced workers needs to be completed to find out if there are special vulnerable groups (e.g., older workers, women, minorities, lesser educated workers) who are falling into poverty and/or having problems in rejoining the workforce. These surveys can also identify what is happening to workers who have used different income support and labor redeployment service.
- *Follow-up on Families and Communities:* Follow-up is normally undertaken using focus groups that attempt to identify the impact of displacement on families and communities, beyond the individual displaced worker. The follow-up of community impact is particularly important in mono-enterprise communities.
- *Gross and Net-Impact Evaluations of Labor Redeployment Programs.* As previously mentioned, both need to be conducted. The first should be built into the performance-based contracts with service providers; the second can be done as a special study on a bi- or tri-annual basis. The first involves defining “performance indicators” for each program, based on the objectives of the program (e.g., increased probability of employment, enhanced wages), then measuring the extent to which program

participants meet these indicators. Performance indicator evaluation systems can help program managers establish targets, provide them with information regarding the degree to which programs are achieving agreed outcomes, provide comparisons between programs and regions, and improve cost-effectiveness of programs. However, performance indicator evaluations do not provide net impact data, as they do not compare participants with similar non-participants. The second evaluation method, which relies on “comparative group design” procedures, does provide net-impact information and can assist program managers and policy makers to make key decisions about program design and implementation. Comparative group design evaluations accomplish this by comparing the degree to which program participants and non-participants, with similar observable characteristics, achieve program outcomes (e.g., do participants in small business assistance programs have a better success rate than non-participants). A number of these evaluations have been successfully carried out in middle-income countries at a modest cost (e.g., US\$150,000) considering the large amount of funds being spent on the programs (Fretwell, 1999).

- *Social Infrastructure:* There is also a need for ongoing monitoring of the divestiture of social infrastructure (e.g., schools, clinics) to ensure that critical infrastructure operated by the SOE is not eliminated with a negative impact on social services. This can usually be done with a simple survey every six months to the SOE involved.

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